

**What comes after the quota went?
Effects of and responses to the ATC expiry**

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Abbreviations

ATC	Agreement on Textiles and Clothing
DfID	Department for International Development
EU	European Union
FES	Friedrich-Ebert-Stiftung
FTA	Free Trade Agreement
FY	fiscal year
GATT	General Agreement on Tariffs and Trade
GDP	Gross Domestic Product
IFI	International Financial Institution
MDG	Millennium Development Goal
MFA	Multi-fibre Arrangement
NTB	non-tariff barrier to trade
PEP	Pakistan Environment Programme
R&D	research and development
RoOs	Rules of Origin
SME	small and medium enterprise
SMEDA	Small & Medium Enterprise Development Authority
SDPI	Sustainable Development Policy Institute
T&C	textiles and clothing
TCP	Trading Corporation of Pakistan
UNDP	United Nations Development Programme
UN-TIHP	United Nations Trade Initiatives from Human Development Perspectives
USA	United States of America
WEBCOP	Workers Employers Bilateral Council of Pakistan
WTO	World Trade Organisation

What Comes After the Quota Went? Effects of and Responses to the ATC Expiry¹

Karin Astrid Siegmann² and Atif Nasim

Abstract

The global environment after the expiry of the quota system in textiles and clothing (T&C) trade poses formidable challenges to human development in Pakistan. Increased quality and price competition in the post-ATC scenario provides an opportunity for some segments of the T&C sector – but a threat to the most labour-intensive ones. As quality and quantity of employment were largely ignored factors in the preparations for the Agreement on Textiles and Clothing's (ATC's) abolition in Pakistan, potential job and wage losses are feared, in garment manufacturing in particular. Unskilled and female workers are most vulnerable.

Challenges also provide the opportunity for change. The following recommendations are put forward in this policy brief:

- *Skills improvement in both skilled and unskilled occupations in the T&C sector should be undertaken by government and industry. This would reduce the vulnerability of these occupations to adverse effects of structural change, and at the same time enhance the competitiveness of the T&C sector.*
- *Likewise, the implementation of core labour standards at the national, regional and global levels would protect, if not improve, working conditions for millions of workers and provide a more level playing field for competition in the post-quota era.*
- *Mitigation measures should be implemented as soon as possible for vulnerable workers who have - or might - become victims of structural change in the T&C industry.*
- *In these efforts, a focus on women workers in skill development and mitigation measures is required. As unskilled workers, women face more precarious working conditions and fewer job alternatives. Very few highly qualified and skilled women enter managerial positions, and this lack is another factor in depriving the country of development opportunities.*
- *Awareness should be raised amongst cultivators and pickers about the health hazards associated with pesticide application. Incentives to reduce cotton contamination should be provided to cotton growers in a manner that can be passed on to female pickers. Such measures would improve working conditions and product value-addition at the same time.*
- *Broadened and strengthened collaboration between workers, employers, and the Government is necessary to reach these objectives.*
- *Overall, social development in Pakistan needs to be emphasised. Investment in, for example, health and education, benefits human development directly, but is also a pre-requisite for more competitive and sustainable industrial development.*

1 This policy brief was compiled with financial support from the United Nations Trade Initiatives from Human Development Perspectives (UN-TIHP). Underlying research received support from the Gender Equality Project, funded by the Department for International Development (DfID), and the Pakistan Environment Programme (PEP). Comments from Aly Ercelan and Foqia Sadiq Khan helped to improve the argument of the paper.

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1. A quantum leap towards freer trade

The Agreement on Textiles and Clothing (ATC) expired in January 2005 and the first year after a quantum leap towards freer trade in textiles and clothing (T&C) has now concluded. The ATC was an agreement under the World Trade Organisation (WTO), aimed at gradually phasing out the quota system that had governed trade in T&C since 1974. Under this so-called Multi-fibre Arrangement (MFA), industrialized countries, mainly the United States of America (USA) and the European Union (EU), placed limits (*i.e.* quotas) on T&C imports for producing countries.

Coming into force in 1995, the ATC phased out this quota system over a ten-year period. Since January 2005, buyers and sellers of T&C products no longer rely on access to quotas in order to sell to the main markets.

The expiry of the quota has given rise to both hopes and fears in the industry. Developing countries, including Pakistan, had lobbied for an end of the quota regime in the Uruguay Round negotiations of the WTO. With high labour surpluses and low labour costs, they rightly perceived themselves as having a comparative advantage in T&C production compared to industrialized nations.

The T&C sector is of great macro-economic importance for several South Asian countries. In Pakistan, it accounts for 9% of gross domestic product (GDP) and about 60% of the country's exports (Ministry of Finance, 2005b). However, the entry of China into the WTO in 2001 signalled the fact that from that point on, a large number of producers across Asia, Latin America, and Africa would have to compete with one huge, cost-efficient producer. It triggered fears of losses of market shares – and millions of jobs (e.g. ITGLWF, 2004).

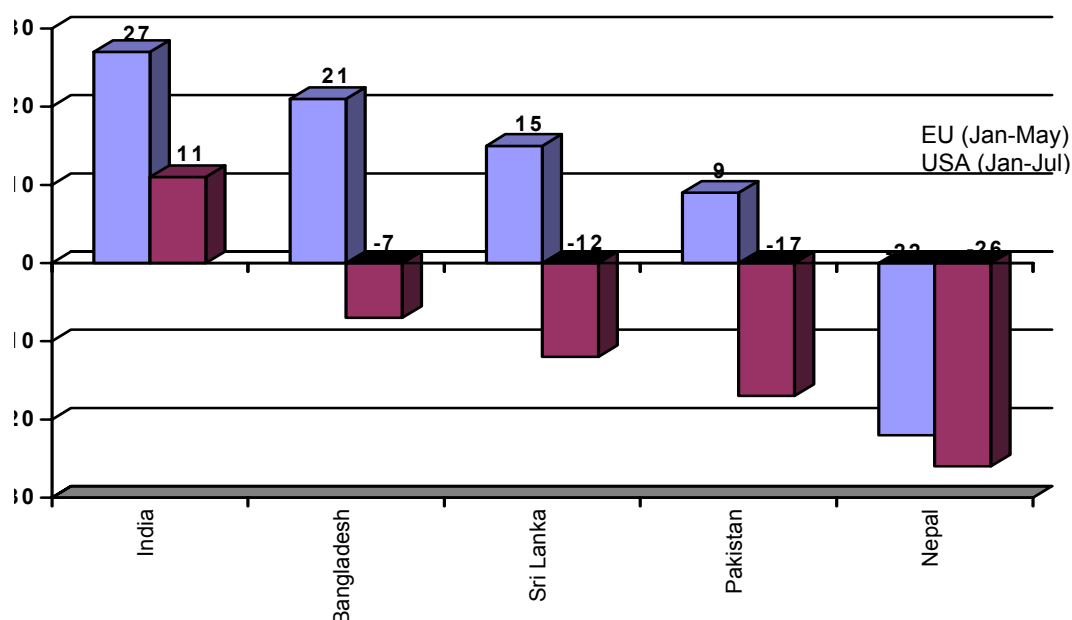
The T&C industry is very labour-intensive. Globally, it employs about 27 million workers (ILO, 2000). It also absorbs a high share of female employment world-wide. Employment in T&C accounts for almost one fifth of the total world female labour force in manufacturing (Joeke, 1995). Overall, women represent 30% of the workforce in the textiles and 75% in the clothing sub-sectors, respectively (Ferenschild and Wick, 2004).

The Pakistani T&C industry employs 35% of industrial sector workers (Ministry of Finance, 2005b). It is estimated that the total workforce in the T&C industry including informal employment totalled 2.3 million in 2000 (Azam, 2004). The largest share of the workforce is employed in garment production and weaving (Khan, 2003). Garment production is also a major employer of women. In stitching units in Pakistan, between 41% and 75% of the total workforce are women (Siegmann, 2005b).

2. What has come after the quota went?

During the first year of freer trade in T&C, some changes in the South Asian economies have already become apparent. Overall, T&C exports have increased. However, this positive broad picture conceals country- and sector- specific effects and damage (Figure 1).

Figure 1: T&C exports 2004 and 2005, selected South Asian countries (% change)



Source: UNDP (2005b)

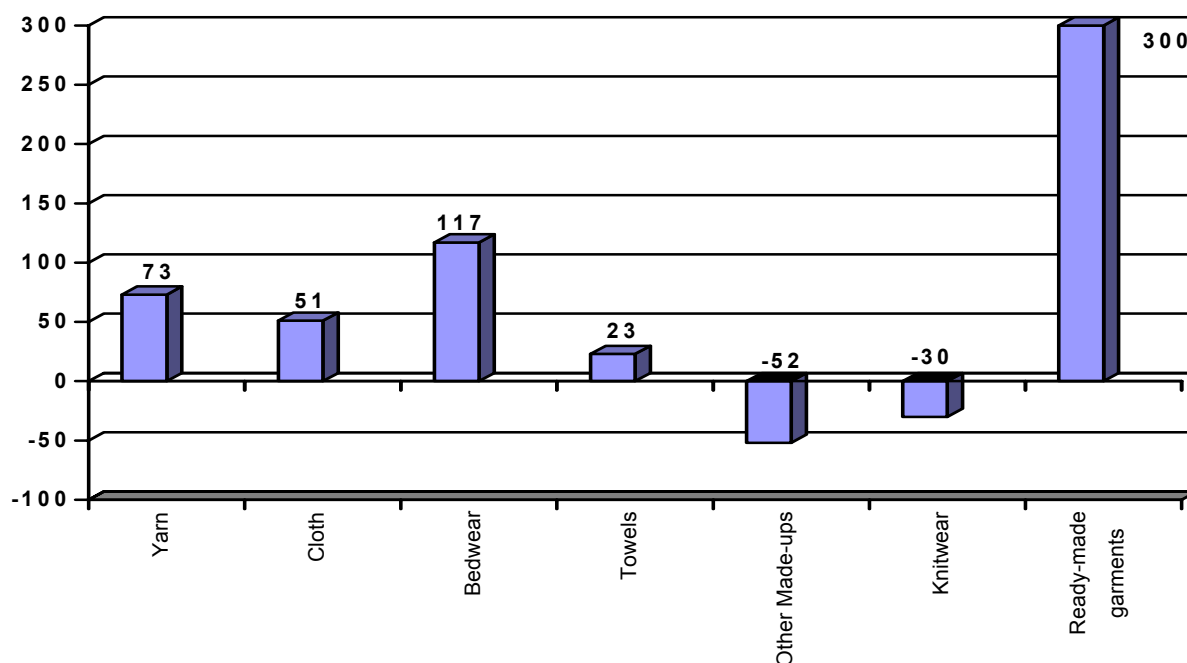
Whereas Bangladesh has been spared the anticipated crash in garments exports, Nepal has lost a significant number of orders from abroad. The reason for the dissimilar performance may lie in a combination of Bangladesh's preferential access to the European market, and the fact that Bangladesh supplies some of the products whose imports are constrained by a recent agreement between the EU and China (Anwar, 2005; EC, 2005; EC, 2004). In recent years the country has invested in backward linkages such as spinning mills and weaving units in order to be able to benefit from duty-free access to the EU market that requires several stages of transformation from raw material to clothing products (Nordås, 2004; Bhattacharya, 1999). In particular, Bangladesh's knitwear exports that had grown significantly between fiscal year (FY) 2003/4 and 2004/5 were supported by domestic incentives in the form of cash compensation schemes and duty drawbacks (Anwar, 2005; Bhattacharya, 1999). Pakistan's and India's textile industries have done well in the post-quota era, but their respective garment sectors have struggled to survive strong price and quality competition after China entered the freer T&C market. As the garment sectors are the most employment-intensive sectors, this might translate into significant employment losses.

At the same time, the intensified competition also puts pressure on wages and working conditions, which were not good even before the opening of the market. Some countries have advocated a relaxation of labour legislation in order to reduce labour costs. For example, Bangladesh has announced that it will increase authorized overtime and relax restrictions on night work by women. Similar legislation is under discussion in India and Pakistan (Ghauri, 2006; ILO, 2005a).

As mentioned above, a first impact assessment of the Pakistani situation shows that the textile sector is doing well, although knit garments in particular are ailing (Figure 2)³.

3 A one year comparison qualifies the extraordinary growth displayed by woven garments. As compared to the period of July-March of the previous fiscal year, ready-made garments showed a growth rate of about 3% (Ministry of Finance, 2005b). The high growth displayed in Figure 2 can be explained by the fall in woven apparel exports in 2004 (Ministry of Finance, 2004).

Figure 2: T&C exports August 2005 (% change vis-à-vis August 2004)



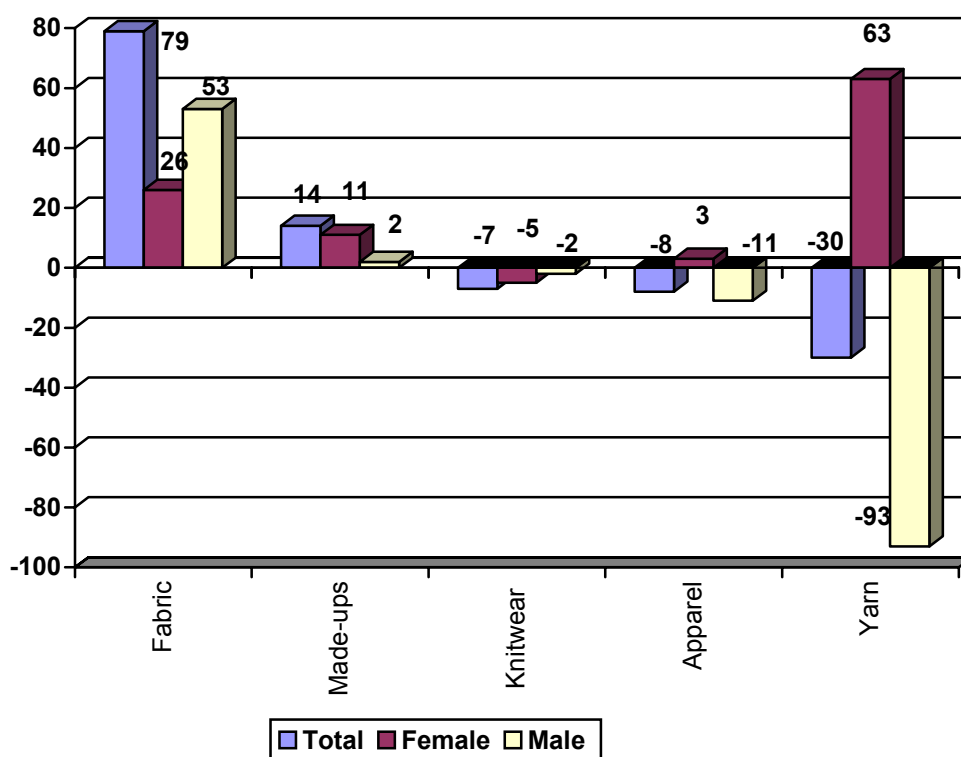
Source: Ministry of Finance (2005b)

A study recently concluded by the Sustainable Development Policy Institute (SDPI) throws light on the reasons for the unexpected growth in sales abroad (Siegmann, 2005a). Capacity increases were the third-most important preparatory strategy for the ATC expiry mentioned in particular by textile exporters. For many companies, selling more is a strategy to cope with prices that have dropped significantly in the post-quota scenario for all product categories, both to maintain profit levels in the short-term and, in some cases, to achieve economies of scale in the longer run. This study's results reveal reduced profits for fabric and apparel companies in particular. Clothing companies interviewed were aware of companies that had gone out of business after the abolition of the quota regime. Thus the question is how sustainable T&C export growth will be.

The rise and fall of sales affects the livelihoods of a great many workers and their dependants. The SDPI study shows that whereas overall employment has slightly increased after the quota expiry, sub-sectoral differences exist (Figure 3)⁴. For exporters of fabric and "made-ups", such as towels and bed-linen, both female and male employment has increased. This reflects their increase in sales abroad. In yarn and apparel production, a replacement of male by female workers has taken place, while total employment has decreased. The on-average lower wages paid to women workers may be part of the explanation. Lower wages help companies to survive in the harsher post-quota competition - albeit on the backs of workers. Finally, knitwear exporters that are still in business have reduced their female as well as their male workforce. Based on the survey results, it is estimated that about 40,000 jobs have been lost in this sub-sector alone in the first year after the quota expired. Industry sources quote an even higher figure (Waleed, 2006).

4 In the interpretation of Figure 3, it is useful to keep in mind the much higher number of garment units than textile units.

Figure 3: Post-quota employment in Pakistan's T&C industry (mean changes)



Source: Siegmann (2005a)

A closer look at the study's results shows that unskilled workers in particular are affected. Male operators who lose their jobs are replaced by unskilled female workers. The slight employment gains in administrative and managerial positions do not benefit women, since men are recruited for these positions.

3. Responses Required

These preliminary trends during the first year after the quota expiry reflect a lack of competitiveness in certain parts of Pakistan's T&C industry. This had been diagnosed long ago. The "Textile Vision 2005", a strategy paper for Pakistan's T&C sector developed in 2000 by the Small & Medium Enterprise Development Authority (SMEDA) identified, amongst other things, the following weaknesses of the sector (SMEDA, 2000): a narrow export product base, with a focus on low-value added yarns and fabrics rather than made-ups and garments, and a lack of focus on a trained workforce in high-value added industries, such as clothing. Increased attention to garments and made-up articles, as well as improved quality throughout the textile chain, was advocated as a response to these challenges. This implied technology upgrading at all stages of textile processing, human resources development, and improved marketing. However, these sound ideas have not been implemented so far.

The impressive amount of USD 5 billion that was invested in the T&C industry between 1999 and 2004 (Ministry of Finance, 2005b) has largely been spent on sectors that are already competitive and not that strongly dependent on exports. Almost half of the investment went into spinning, while the woven and

knit garments sectors obtained less than 5% of the total (Ministry of Finance, 2004), *i.e.* about one third of the investment targeted in the “Textile Vision 2005” (Ministry of Finance, 2003). In many cases, the investment was labour-saving (Siegmann, 2005b). Overall, this means that employment and the skills of the workforce have been neglected in the preparations for the quota expiry, even where these would have increased the industry’s competitiveness.

This situation might deteriorate further in the mid-term. The following post-ATC scenarios for Pakistan’s T&C industry’s development are conceivable. One option is further specialization in yarn, cloth, and made-ups. The alternative is the move towards higher value addition that is also advocated by the “Textile Vision 2005” (Siegmann, 2005b). Given the current skill and gender structure in employment, both scenarios imply reductions in unskilled and female work.

The structural change in T&C trade induced by the lifting of the quotas has been slowed down by the responses of the USA and EU to curb Chinese T&C imports to their respective economies. The EU has limited Chinese textile exports in 10 categories of concern to agreed growth levels until the end of 2007 (EC, 2005). An agreement between the USA and China, signed in November 2005, places quotas on 34 product categories of Chinese textile and clothing exports to the US until the end of 2008 (GoUSA and GoPRC, 2005). This gives some more breathing space to deal with the challenges of the ATC abolition for Pakistan’s economy and economic development.

4. Decent work in globally competitive jobs⁵

One of the most important steps to be undertaken is to strengthen product quality by investing in workers’ skills and research and development (R&D). With special emphasis on small and medium enterprises (SMEs), which form a large portion of garment and cloth manufacturers, this is also stressed by the Planning Commission’s “Medium-Term Development Strategy 2005-2010” (Planning Commission, 2005). As mentioned above, relaxation of labour legislation increases capital productivity but the need is to increase labour productivity for successful competition with China. In order to achieve this, workers, employers and government should join hands to improve both competitiveness and working conditions. An example of an existing bipartite forum is the Workers Employers Bilateral Council of Pakistan (WEBCOP). Consultations such as this need to be broadened and strengthened. Within the T&C industry, better-trained operators can reduce wastage, produce higher quality products, and support pro-active product development and marketing, especially in high value-added product categories. Besides strengthening the industries’ competitiveness, enhancing workers’ skills would support their bargaining power. Better skills increase their chances of finding job alternatives within and outside the T&C industry and thus potentially benefits Pakistan’s overall industrial development. Ways to achieve this may include on the job skill development and more and improved training institutes targeting operator-level T&C workers, with preferential enrolment for women. Female workers comprise a large share of T&C workers in made-ups and garments, in particular in the informal sector (Khan, 2001). Clearly, in the short term their employment has increased. For this reason and because of female workers’ greater vulnerability due to poorer education and fewer job alternatives, it is crucial that their skills are enhanced.

5 Many of the recommendations below were developed during two strategic workshops initiated by SDPI. One, jointly organised by SDPI and Friedrich-Ebert-Stiftung (FES), took place in October 2004 with representatives of workers’ organisations (SDPI and FES, 2004). The second one, sponsored by the UN-TIHP, brought together stakeholders ranging from business representatives, via government officials to trade unionists from across South Asia in November 2005 (SDPI and UN-TIHP, 2005a).

Also, the lack of skilled workers has been identified as a bottleneck for the industry's development (Khan, 2005), in particular in the garments industry. That is why managerial skills which requires development. In particular, women's entry into administrative and managerial positions should be facilitated. National and international statistics show that female students outperform their male colleagues both in school and at university. The almost complete lack of women in skilled occupations means the Pakistani T&C remains far below its potential (SDPI and UN-TIHP, 2005b).

In skill development both for unskilled and skilled labour, industrialised countries can and should support the transition to freer trade in T&C through both bi-lateral and multi-lateral aid. Importing industrialized countries benefit from the quota expiry and have taken responsibility for reaching the Millennium Development Goals (MDGs) that include developing global partnerships for development.

In cotton cultivation, enhanced product quality means incentives to reduce contamination (*i.e.* with jute or polypropylene fibres, human hair and pesticides). Contamination has been identified as one of the major obstacles to increased sales for Pakistan's cotton and cotton products. Reducing contamination can easily be achieved if cotton pickers are paid incentives for uncontaminated cotton. A decision was recently taken to provide these incentives through the Trading Corporation of Pakistan (TCP). If implemented, this might translate into better pay for cotton pickers since they ultimately control this type of contamination (No author, 2006). Reducing the levels of pesticide contamination by awareness raising amongst cotton growers and incentives for growing organic cotton as stipulated in the Trade Policy 2005/6 (Ministry of Commerce, 2005) would not only enhance the prospects of Pakistani T&C exporters to enter niche markets for environmentally friendly cotton products. First and foremost, it would reduce the significant health hazards cotton pickers, their families and communities are exposed to (Hussain, 1999).

Overall, Pakistan needs to strengthen its investment in social development, *e.g.* in the areas of health and education. In the 2005-06 budget, these two areas account for a meagre 0.4% and 1.5% of public expenditures, respectively (Ministry of Finance, 2005a). Spending in these areas serves national human development directly, but also supports sustainable industrial development that is less vulnerable to pressure from industrialised countries. It may include incentives for industrial diversification away from concentration on T&C production that has made Pakistan and other T&C producing countries extremely vulnerable to changes in the global trade environment.

In order to better protect T&C workers against becoming a buffer for intensified trade after the quota expiry, the government and employers need to do a number of things: implement existing labour laws; extend them to contract and informal sector workers and to workers in export-processing zones, and introduce sanctions against violations of those laws. A recent SMEDA study shows that, rather than is commonly perceived, the costs of compliance are not excessive. For an average SME, estimated costs for compliance with labour legislation are not expected to exceed 1.5-2% of annual turnover (SMEDA, 2002). Women workers are particularly vulnerable due to their concentration in precarious types of work, such as piece-rate contracts and home-based work. The ILO might be able to assist the implementation of these suggestions (Box 1). International financial institutions (IFIs) such as the World Bank and the Asian Development Bank need to be persuaded that their enormous and increasing lending for industry remains a special opportunity to leverage this aid into expanding decent work.

Box 1: Better Factories Cambodia

The ILO engaged in a project in Cambodia whereby garments factory conditions would be monitored and the USA would reward Cambodia with bonus quotas in return for measurable improvements in working conditions. The project was known as “Better Factories Cambodia” and also included training on working conditions and other topics. It extended to all garment-exporting companies, and proved successful because the transparency of the monitoring made it credible to international buyers. After the USA-Cambodian trade agreement ended in 2004, Cambodia continued its efforts to improve factory conditions since Cambodia’s key overseas buyers rated labour standards as a top priority in their decision to source from them. Furthermore, they indicated that improved work standards benefited workplace productivity and product quality. This model may prove reassuring to companies concerned that improving work standards would be an unjustified expense. Early data indicates that the programme has allowed most of the garments industry to survive the end of the quota regime and to maintain buyer loyalty. However, a report published in April 2005 discusses the increasing pressure being put on trade union rights outside the factories, which may potentially tarnish the industry’s international image.

Source: ILO (2005a)

Given the increased role of non-tariff barriers to trade (NTBs), such as Rules of Origin (RoOs), Free Trade Agreements (FTAs) and preferential market access, the potential costs involved have less bearing on short-term competitiveness (Kulkarni, 2005), but enhance it in the mid and long term. This is because increased quality competition in the post-ATC scenario requires a motivated workforce and decent working conditions. Equally, social and environmental certification of products and processes has become a competitive factor, especially for garments exporters.

Labour standards should also be enforced at the regional and international level. Minimum standards for duty-free access of employment-intensive Pakistani garments to markets of industrialised countries should be included in bilateral trade agreements in exchange for special regard for labour standards (Box 1). Globally, implementing the ILO core conventions at the level of the WTO provides a more level playing field for competition, enhances competitiveness, and benefits millions of workers.

The post-ATC scenarios outlined above imply that special mitigation strategies are needed for unskilled garments workers, most of whom are female. In particular, the government and employers share a responsibility to set up targeted social safety nets for workers who are dismissed due to the ATC expiry (SDPI and FES, 2004, SDPI and UN-TIHP, 2005a). They may include counselling, skill upgrading, entrepreneurship programmes, access to loans etc. A special effort should be made to reach vulnerable female workers, because they face significantly lower chances of finding alternative employment. Bangladesh, for example, planned to train 40,000 garments workers to improve their skills together with a non-profit organisation (UNDP, 2005a). The ILO TREE programme for skill development implemented in two districts of Pakistan may also serve as a model (Box 2).

Box 2: Skill development for vulnerable groups

The Training for Rural Economic Empowerment (TREE) programme is an ILO project aimed at creating employment opportunities for vulnerable social groups, essentially through skills training and other support services.

The first step within TREE is the identification of economic opportunities. This includes undertaking a detailed situation analysis to gather information on the basic profile of the area selected. This is followed by feasibility studies to identify viable (self) employment and income generation opportunities.

The training is designed thereafter. The curriculum is reviewed and, if needed, modified according to the requirements of the identified economic opportunities. The training providers also give on-the-job training to graduates in their workplaces whenever required. In view of the very low literacy levels of the beneficiaries, especially women, training in functional literacy and basic numeracy is also provided.

The training needs of the beneficiaries are addressed through an integrated menu of support services. This includes formation of groups and associations, micro-finance services, training in management and leadership, advisory services, linkages with technology resources, on the job training, and linking with and mainstreaming into local economic development programmes.

The outcomes of the TREE methodology in terms of employment creation have been quite satisfying. A central achievement of the project is its success in mitigating the socio-cultural and mobility constraints faced by women. The overall female participation is 56% in skills training and literacy programmes. More generally, around 91% of the beneficiaries who received training under the project have already been employed and are using their skills to generate incomes.

Source: ILO (2005b)

At the multilateral level, the WTO can provide technical assistance to mitigate the social costs of the industry's restructuring, so as to develop, strengthen, and diversify the country's production and export base. This would be an effort to balance the strongly biased distribution of costs and benefits of the ATC: a bias which benefits consumers and transnational corporations in the North, while hurting producers and – in particular - their workforce in the South.

5. Towards sustainable industrial and human development in the post quota era

The global environment after the expiry of the quota system in T&C trade poses formidable challenges to human development in Pakistan. Increased quality and price competition in the post-ATC scenario is an opportunity for some segments of the T&C sector – but a threat to the most labour-intensive ones. As the quality and quantity of employment were largely ignored factors in the preparations for the ATC abolition in Pakistan, potential job losses are feared, especially in garments. Here, too, unskilled and female workers are most vulnerable.

Challenges also provide the opportunity for change. The following recommendations have been put forward in this policy brief:

- Skill improvement in the T&C sector should be undertaken in both unskilled and skilled occupations. This would reduce their vulnerability to the adverse effects of structural change, and at the same time enhance the competitiveness of the T&C sector.
- Likewise, the implementation of labour standards at the national, regional and global levels would improve working conditions for millions of workers and provide a more level playing field for competition in the post-quota era⁶.
- Mitigation measures should be implemented as soon as possible for vulnerable workers who have or might become victims of structural change in the T&C industry.

6 For a useful overview over Pakistan's labour legislation with special reference to SMEs and suggestions for enhanced implementation, see PILER (2005).

- In these efforts, a focus on women workers in skill development and mitigation measures is recommended. As unskilled workers, women face more precarious working conditions and fewer job alternatives. Very few highly qualified and skilled women enter managerial positions, and this lack is another factor in depriving the country of development opportunities.
- Incentives to reduce cotton contamination should be provided to cotton growers and passed on to female pickers. Awareness should be raised amongst cultivators and pickers about the health hazards associated with pesticide application. Such measures would improve working conditions and product value addition at the same time.
- Broadened and strengthened collaboration between workers, employers, and the Government is necessary to reach these objectives.
- Overall, social development in Pakistan needs to be emphasised. Investment in health and education benefits human development directly, but is also a prerequisite for more competitive and sustainable industrial development

Glossary

Agreement on Textiles and Clothing (ATC): WTO agreement established in the Uruguay Round which provided for the gradual dismantling of the quotas that existed under the Multi-Fibre Arrangement. The ATC expired on January 1st 2005.

Apparel: Anything that has been manufactured into use for clothing.

(Environmental/Social) Certification: Proof that an environmental/social management system has been introduced and works. Certification is carried out by specially appointed companies that continually monitor the activity.

Clothing: relates to made-up articles, wholly or chiefly of textile materials, commonly to be worn on a human body.

Free trade agreement (FTA): An arrangement which establishes unimpeded exchange and flow of goods and services between trading partners regardless of national borders.

ILO Conventions: Eight ILO conventions have been identified by the ILO's Governing Body as being fundamental to the rights of human beings at work, irrespective of levels of development of individual member States. They are legally binding as they have been ratified by the member states.

Knitwear: Clothes made by connecting wool or another type of thread into joined rows. Examples are T-shirts, socks, underwear.

Made-ups: Non-clothing related items such as towels, bed linen, and other products.

Millennium Development Goals (MDGs): A set of eight time-bound and measurable goals and targets for combating poverty, hunger, disease, illiteracy, environmental degradation and discrimination against women. They are a blueprint agreed to by all the world's countries and all the world's leading development institutions, under the auspices of the United Nations.

Multi-Fibre Arrangement (MFA): An agreement which governed the world trade in textiles and garments from 1974 through 2004, imposing quotas on the amount developing countries could export to developed countries. It expired on 1st January 2005.

Quota: In trade terms, a restriction of imports of a commodity to a specific quantity.

Rules of Origin (RoOs): Rules included in a Free Trade Agreement (FTA) specifying when a good will be regarded as produced within the FTA, so as to cross between members without tariff. Typical RoOs are based on percentage of value added or on changes in tariff heading.

Textile: Textiles are woven or knit fabric, made from natural or synthetic fibres, filaments or yarns, suitable for further processing into apparel.

World Trade Organization (WTO): An international rules-based and member driven organization which oversees a large number of agreements defining the "rules of trade" between its member states. The WTO is the successor to the General Agreement on Tariffs and Trade (GATT) that was set up in 1947, and operates with the broad goal of reducing or abolishing international trade barriers.

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